SUPREME COURT, U. S.

OCT 1 1957

JOHN F. DAVIS, CLERK

In The

Supreme Court of the United States

October Term, 1957

No. 716

WILLIAM R. JACKSON,
WILLIAM R. & ALICE J. JACKSON,
CLEVELAND CHAIR COMPANY,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

RICHARD P. LAHR
ROBERT A. SMITH
1211 Penton Building
Cleveland 13, Ohio

Attorneys for Petitioners

TABLE OF CONTENTS

	Page
OPINIONS BELOW	2
JURISDICTION	3
QUESTIONS PRESENTED	3
STATUTE INVOLVED	6
STATEMENT OF THE CASE	7
REASONS FOR GRANTING THE WRIT	25
Introductory Statement	25
Question One	28
Question Two	34
Question Three	39
CONCLUSION	43

INDEX TO APPENDIX TO PETITION

APPENDIX A:	
Sixth Circuit's Opinion	A1
Sixth Circuit's Judgments	A8-A10
Excerpt from Government's Brief in Sixth Circuit	A11
APPENDIX B: (In separate Volume)	
(Detailed Table of Contents at Beginning of Separate Volume)	
Copies of Certain Exhibits	1083a-1179a

Memorandum Findings of Fact and Opinion of the Tax Court of the United States, (Dockets Nos. 70811; 70812; 70813; 70814) 1183a

Decision (Docket No. 70811) 1250a

Decision (Docket No. 70812) 1253a

Decision (Docket No. 70813) 1255a

Petition for Review (Docket No. 70811). 1257a

Petition for Review (Docket No. 70812). 1259a

Petition for Review (Docket No. 70813). 1261a

CASES CITED

Burnet v. Houston, 283 U.S. 223 (1931) 26, 41

Bryan v. Comm., 209 F. 2d 823 (5th Cir. 1954) 28

Jack M. Chesbro, 21 T.C. 123 (1953) aff'd per curiam, 225 F. 2d 674 (2d Cir. 1955 37

Cirillo v. Comm., 314 F. 2d 478 (3d Cir. 1963) 35, 42

Clark v. Comm., 226 F. 2d 698 (9th Cir. 1959) 37

Cohen v. Comm., 226 F. 2d 265 (5th Cir. 1959) 33

Consolidated Edison Co. v. NLRB., 305 U.S. 197, 230 (1938) 31

Corn Products Refining Co. v. Comm., 350 U.S. 46 (1955) 25

Cullers v. Comm., 237 F. 2d 611 (8th Cir. 1956) 33

Delone v. Comm., 100 F. 2d 507 (3rd Cir. 1938) 26

Contents Continued

Page

E. C. Dodd, T.C. Memo. 1962-235, 21 T.C.M., 1261 ..... 8, 9
Drieborg v. Comm., 225 F. 2d 216 (6th Cir. 1955) 16, 35
J. D. Farber, 43 T.C. 407, Dec. 27,201 31
George v. Comm., 388 F. 2d 221 (1st Cir. 1964) 35, 42, 43
Goldberg v. Comm., 239 F. 2d 316 (5th Cir. 1956) 42
Grubb v. Comm., 315 F. 2d 753 (6th Cir. 1963) 29, 37
Harp v. Comm., 263 F. 3d 139 (6th Cir. 1959) 29, 30
Helvering v. Taylor, 293 U. S. 507 (1935) 25, 28, 29, 30, 31, 33, 34
Hoffman v. Comm., 298 F. 2d 784 (3rd Cir. 1962) 31
Kreps v. Comm., 351 F. 2d 1 (2d Cir. 1965) 28, 35
Lloyd J. Lowe, T. C. Memo 1955-150, 14 T.C.M. 547 36
MacCrowe's Estate vs Comm., 252 F. 2d 293 (4th Cir. 1958) 34
Masters v. Comm., 243 F. 2d 335 (3d Cir. 1957) 37
Richardson v. Comm., 264 F. 2d 400 (4th Cir. 1959) 35, 37, 39
Ries v. U. S. 172 F. Supp. 929 (E.D. Pa. 1959) 36
Tank v. Comm., 270 F. 2d 477 (6th Cir. 1959) 38
Thomas v. Comm., 266 F. 2d 297 (6th Cir. 1959) 29
United Aniline Co. v. Comm., 316 F. 2d 701, 704 (C.A. 1st) 32, 33
U. S. v. Lefkoff, 113 F. Supp. 551 (E.D. Tenn. 1953) 9

Welch v. Comm., 297 F. 2d 309
(4th Cir. 1961) 29, 30

STATUTES CITED

26 U.S.C.; Section 6501(a) 7
26 U.S.C., Section 7454 6
28 U.S.C., Section 7482 3
Internal Revenue Code of 1939, Sec. 1112 6

MISCELLANEOUS

Shepard's United States Citations 25

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No.

WILLIAM R. JACKSON,
WILLIAM R. & ALICE J. JACKSON,
CLEVELAND CHAIR COMPANY,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

Petitioners pray that a writ of Certiorari issue to review the Judgment entered July 14, 1967, by the United States Court of Appeals for the Sixth Circuit (hereinafter called

"Sixth Circuit") in Case Nos. 17023, 17024, and 17025 in that court, filed by the above captioned Petitioners respectively against the Respondent, and consolidated for hearing, decision and judgment. The said judgment of the Sixth Circuit affirmed decisions entered August 3, 1965 in the Tax Court of the United States in the three cases (Docket Nos. 70811, 70812 and 70813 in the Tax Court) in favor of Respondent, for tax deficiencies and fraud penalties, which total approximately $1,400,000.00 to date including interest.

A certified transcript of the record in said cases (including the proceedings, opinion and judgment in the Sixth Circuit, and a joint appendix filed with said court), is furnished herewith in accordance with this Court's Rules.

OPINIONS BELOW

The Sixth Circuit's Opinion appears in Appendix A to this Petition at A1-A7. * The Opinion has not been officially reported, so far as Petitioners have been able to determine at the time of printing, but is unofficially reported in 67-2 USTC Para. 9557.

The Memorandum Findings of Fact and Opinion of the Tax Court of the United States is officially designated as T.C. Memo 1964-330 filed December 23, 1964, and is unofficially reported at 23 T.C.M. 2022. The Tax

---

* The page references to Appendix A to this Petition will be designated, e.g. "A3".

Court's said Memorandum Findings of Fact and Opinion is to be found in separate Appendix B hereto beginning at page 1183a. **

JURISDICTION

The Judgment of the Sixth Circuit was dated and entered on July 14, 1967 (A8-A10). The jurisdiction of this Court is invoked under 28 U.S.C., Section 7482.

QUESTIONS PRESENTED

1. In a tax fraud case, the taxpayers freely admitted that the gross sales of their two furniture manufacturing businesses had been understated on their tax returns in each of certain years in question during World War II, but claimed offsetting and previously unclaimed deductions by reason of the use of the proceeds of these unreported sales to make purchases of raw materials on the "Black Market". Both the Tax Court and the Sixth Circuit found proof of existence of fraud but

---

** Appendix B hereto is a separate volume which is the same as Volume III of the Certified Joint Appendix (pages 1093a-1263a) in the Sixth Circuit. It contains copies of certain important Exhibits in addition to the Tax Court's Memorandum Findings of Fact and Opinion, Decisions, and the Petitions for Review to the Sixth Circuit. Page references to Appendix B, as well as to the entire Certified Joint Appendix, will be designated, e.g. "1183a". Any reference to 1093a or above, may be found in Appendix B hereto, as well as correspondingly in said Certified Joint Appendix.

also found that Respondent's determination of deficiencies, making no allowance for offsetting deductions for Black Market purchases, was erroneous. The Sixth Circuit nonetheless held that the burden of proof as to the claimed Black Market deductions was on the taxpayers, which they had failed to carry, and hence sustained Respondent's deficiency determinations as adjusted by the Court. The first question presented is:

Whether the taxpayers, having shown the Respondent's deficiency determinations to be erroneous, had the further burden of proving they owed nothing (through proof of the claimed Black Market deductions), or if liable at all, the correct amount?

2. In the same tax fraud case, customer checks representing the omitted gross sales were endorsed in bearer form by one or the other of said businesses and all were claimed by taxpayers to have thereupon been cashed at the bank with the assistance of its manager, with the cash being used for Black Market purchases not previously claimed as deductions. An analysis of such bank records as were available by the government, however, established that many of these checks were ultimately deposited in "fictitious" savings accounts at said bank and that out of $530,000.00* in net deposits to said accounts, $184,000.00* was traceable back into the hands of the taxpayers. Taxpayers explanation was that the bank manager, unbeknownst to taxpayers at the time, had control of large sums not belonging to the bank (the Tax Court so found in the bank manager's own case), which he used to cash said customer checks, and thereafter

---

*Approximate figures

deposited said checks in said fictitious accounts which he had established and controlled. Similarly, taxpayers explained, but the lower courts declined to believe, that the $184,000.00 represented in some instances sums due from the bank manager on business transactions which he chose to satisfy by withdrawals from his fictitious accounts, and in other instances represented what at the time were believed to be routine bank borrowings, but actually were loans made by the bank manager personally by withdrawals of his private funds from said fictitious accounts. Obviously, if the claimed offsetting Black Market purchases were in fact made, then the taxpayers rejected explanations must be accepted, because having received and spent the cash, they could have had no interest in the cashed checks when deposited in the fictitious accounts. Under such circumstances, the second question presented is:

Whether, in imposing the burden on the petitioners of proving the claimed Black Market expense deductions, the Sixth Circuit erroneously relieved the respondent of his burden in a tax fraud case of proving the opposite by clear and convincing evidence, which he made no effort at the trial to carry, and without carrying which, there was no basis other than speculation for concluding that the funds in the fictitious accounts belonged to petitioners?

3. In the same tax fraud case, the Sixth Circuit strongly indicated agreement with taxpayers that the evidence was not clear and convincing upon which the Tax Court found that only $100,000.00 should be allowed taxpayers as a deduction for previously unclaimed Black Market purchases, no part of which had been allowed in the Government's erroneous deficiency determinations. The Sixth Circuit reasoned, however, that the proof of $184,000.00 in withdrawals from the fictitious accounts being traceable into petitioner's hands and thereafter expended for personal purposes, established that some portion of the tax deficiencies asserted was due to fraud,

thereby placing the burden of proof on the taxpayers of setting aside as erroneous the Commissioner's redetermination of taxes as adjusted by the Tax Court. Again, if the full amount of offsetting deductions claimed by the taxpayers was correct, there could be no valid basis for finding that the $184,000.00 belonged to the taxpayers when withdrawn from the fictitious accounts, and hence that the taxpayers were guilty of tax fraud. The third question presented accordingly is:

Whether, when the government's tax deficiency determinations are found to be erroneous by reason of a failure to allow offsetting deductions for Black Market purchases, and there is no clear and convincing evidence upon which to base a finding as to the correct amount of such deductions as being less than the full amount claimed by taxpayers, the government may nonetheless be allowed the benefit of inferences from secondary facts (the $184,000) to place the burden of proof as to primary facts (Black Market deductions) upon the taxpayer, when the validity of the Government's contentions as to said secondary facts is totally dependent upon the correct finding as to the primary facts?

STATUTE INVOLVED

26 U.S.C., Section 7454 provides in part as follows:

> "(a) Fraud.--In any proceeding involving the issue whether the petitioner has been guilty of fraud with intent to evade tax, the burden of proof in respect of such issue shall be upon the Secretary or his delegate".

Similar provisions to this section were contained in Section 1112 of the 1939 Internal Revenue Code.

STATEMENT OF THE CASE

The Petitioners in these three consolidated cases sought review respectively by the Tax Court, and later by the Sixth Circuit, of Income Tax deficiencies and fraud penalties asserted against Petitioners William R. Jackson and Cleveland Chair Company for the years 1942 through 1945, and income tax deficiencies against Petitioners William R. Jackson (hereinafter referred to as "Jackson"), and his wife, Alice J. Jackson, (hereinafter referred to as "Alice") for the years 1948 and 1949. Originally the years 1941-1947 were involved as to Alice, and 1941 and 1946-1947 as to Jackson, but the Tax Court found for Petitioners in those years, after the Government conceded 1941 (1184a, 1230a-1231a, 1246a).

The deficiencies all stemmed from allegedly unreported net income from two furniture manufacturing businesses, the one being Petitioner Cleveland Chair Company, a corporation owned 55%-45% by Jackson and Alice, and the other being Jackson Manufacturing Company, a 55%-45% partnership between Jackson and Alice until its incorporation in 1946 (1187a-1188a, 1221a).

The years other than 1948-1949 were barred by the Statute of Limitations (26 U.S.C., Section 6501(a)) unless fraud could be established (1184a, 1231a). 1948-1949 involved only de minimis amounts (1183a) representing interest on certain "fictitious" bank savings accounts established during World War II which the Government contended Jackson and Alice owned, and which ownership they denied (1222a, 1223a, 1236a, 1246a-1248a). The events decisive of this litigation all occurred in the years 1942-1945 (1190a-1213a).

The Tax Court filed elaborate memorandum findings of fact (1185a-1230a). The Sixth Circuit stated that it had no ground for determining that any of these findings of fact were clearly erroneous and incorporated same in the Sixth

Circuit Opinion by reference (A5, A7). Petitioners did not and do not now question said findings of fact, except to the extent they infer ownership in Petitioners of the funds in the fictitious accounts; limit offsetting Black Market purchases to $100,000.00 (1217a, 1221a, 1222a); find that Jackson did not use diverted funds for purchases of materials (1219a); and attribute omissions of net income to Petitioners (1222a). Petitioners further questioned and do here question the "ultimate facts" as found by the Tax Court insofar as adverse to them (1230a-1231a).

As shown by said Findings of Fact, gross income from sales of the two furniture manufacturing businesses involved was omitted from the pertinent tax returns during certain years in World War II (1194a). The Petitioners contended that the customers' checks in question had been cashed at the East Chattanooga Branch of the Hamilton National Bank of Chattanooga with the assistance of one E. C. Dodd (hereinafter referred to as "Dodd"), the branch manager, and that the resulting cash was used to make purchases on the Black Market and otherwise of raw materials for use in the businesses (1194a, 1216a). It was Petitioner's contention that the omitted sales were completely offset by said purchases, which were also omitted from the tax returns in question; hence, although gross income was freely admitted to have been understated, net income was correctly reported (9a, 45a).

The Government discovered that something was substantially amiss at the East Chattanooga Branch of the Hamilton National Bank of Chattanooga and began an intensive investigation in 1950 (190a-191a, 357a-358a, 368a). The branch manager, the said Dodd, resigned suddenly and "the place was swarming with Internal Revenue Agents" (190a-191a). Dodd was ultimately found by the Tax Court in his own case (See 1237a) to have been guilty of tax fraud for the years 1942-1949 by not reporting a total of approximately $78,500.00 in income he had earned from "a separate operation, a business of making cash loans out of private funds placed at his disposal for that purpose". E.C. Dodd,

T. C. Memo 1962-235, 21 T.C.M. 1261, 1264.

The Tax Court further found that "certain depositors" permitted Dodd to use their funds to make these "side-line" loans "during his normal working hours at the bank without the knowledge or permission of the other bank officials", and that he "used his position at the bank" to accomplish his purposes. The Government's first inkling of the situation came when Dodd was contacted by an agent investigating another taxpayer "to verify a deduction the other taxpayer had taken on his tax return for interest claimed to have been paid on a loan from the bank". Dodd thereupon promptly made a voluntary disclosure of his omitted income. 21 T.C.M. 1261 at 1263.

Proof was offered at the trial by a CPA who had personally borrowed from time to time from what he thought was the branch bank, through Dodd, signing a series of notes payable to the bank. These notes were ultimately determined at the time of the Government's investigation, to be owed in fact to one Lefkoff, whose attorney ultimately collected the notes from the CPA. (670a-676a; Exhibit 64 and 65). Lefkoff, incidentally, also had his problems (criminal tax fraud) as a result of the Government investigation: See 354a-355a; 358a, 378a, and U. S. v. Lefkoff, 113 F. Supp. 551 (E.D. Tenn. 1953).

The Government investigators acknowledged that while Dodd had admitted an arrangement with others (Lefkoff) with respect to "the diverting of sales", he stated to them at the outset that "no such arrangement existed" with Jackson (377a-378a).

The Tax Court found that Jackson, through his businesses, had become the largest depositor at the branch bank; that he had a close and highly informal banking relationship with Dodd (See e.g. 891a-892a); that he had borrowed from time to time from the branch bank through Dodd; and that "Jackson trusted Dodd and accepted advice from him on financial matters"(1220a).

The Tax Court also found that "some time during the years here involved, Jackson turned over to Dodd the handling of his private loans. From time to time Dodd would account to Jackson for collections on these loans" (1220a-1221a; See also 1247a).

Petitioners introduced into evidence a signed acknowledgment from Dodd to Jackson dated in May of 1946 showing he was under a duty to account to Jackson at that time for $31,344.87 (822a-824a; 826a-832a, Exhibit 58, 1144a).

The Tax Court also found that in order to finance the Black Market Purchases, it was with Dodd that arrangements were made by Jackson for an employee of the businesses, W. E. Wooten, to cash customers' checks payable to the businesses, without being deposited to the regular company accounts (1216a; see also 495a-496a and 736a-737a). The Tax Court further found that Wooten would ask Dodd to "hold the cash for a day or two until he called for it" and that Black Market purchases at one time by Wooten "never exceeded $25,000.00" (1216a-1217a).

The government investigation of Petitioners as such began in November of 1951 (368a-369a), some 7 to 9 years after the critical events in question. Suit was filed in the Tax Court in late 1957 (1a, 25a, 39a) and the cases were tried by the Tax Court in 1963 (71a) twenty years after the key year of 1943. In the meantime, virtually all of Petitioners' records for the principal years in question (1942-1945), including accurate records kept of omitted sales and purchases, (495a-498a, 502a, 736a-739a, 947a-948a, 966a, 994a, 1067a-1068a) were destroyed as a result of water damage caused by both fire and flood, under circumstances the innocence of which the government investigators did not question (290a, 359a, 470a, 503a-504a, 609a-614a, 637a, 708a-710a, 789a-794a, 1194a). Such pertinent records as any of the Petitioners had, either business or personal, still available to them (1082a), were fragmentary, being itemized in Exhibit 59 (1145a). There was no proof in the record to suggest any basis for suspicion or criticism for the failure of any of the

Petitioners to have retained and preserved material records.

With the passage of time, Petitioners' original counsel, Albert Taber (882a), became deceased, and later, their original chief counsel of record in the tax court, Joe Roddy, and numerous important witnesses as well (93a, 752a, 812a, 949a, 1046a, 1082a).

The government investigations revealed that a series of savings accounts had been opened in "fictitious" names at the branch bank, which names had relation to Jackson's family or others close to him (1201a). It further traced into these accounts a substantial number of out-of-town checks endorsed by one or the other of the two businesses, although all deposits to these accounts could not be identified (1195a-1201a; 1202a-1210a). Some $530,000.00 in all was deposited to these accounts exclusive of transfers between accounts (1195a-1209a, Exhibit 52, 1129a-1137a). By further analysis of bank records, the government determined that some $184,000.00 of these deposits were traceable back to Jackson for personal use in seven different transactions (1211a-1214a).

Jackson denied any connection from the beginning with the fictitious accounts other than the Thomas Rogers account, a special case (1236a, 534a-535a, 538a-539a, 741a-744a, 998a-1000a), "right down the line, through counsel and on his own behalf before obtaining counsel (378a). Jackson's explanations (843a-913a) for the apparent open and shut case against him resulting from the discovery of the seven transactions were never discussed by the Tax Court or the Sixth Circuit. The Tax Court in a very lengthy opinion devoted only one sentence to disposing of the detailed explanatory proof offered by Petitioners (1234a-1235a):

> "We have not set forth in detail the various explanations which Jackson attempted to give since they are so inconsistent and confused as to be totally unworthy of belief."

Jackson contended that while the $184,000.00 may well have been directly traceable back to him from the fictitious accounts as the government's proof showed, that in all cases the answer was that Dodd, unbeknownst to Jackson, had been using the funds in these accounts which he controlled, and not Jackson, to either loan money to Jackson in what Jackson thought were routine bank borrowings, or in other cases, to account to Jackson for sums due from Dodd on financial transactions Dodd was handling for Jackson (1234a).

While it is recognized that this court's proper function with respect to review of the evidence is very limited after both the Tax Court and the Sixth Circuit have reviewed same, nonetheless, because of its underscoring of the critical relation of the burden of proof question to a proper decision in these cases, the attention of this Court is called to one illustrative instance of the type of explanatory proof the Tax Court so summarily rejected.

The major item in the seven transactions aforesaid was a tracing of the sum of $100,000.00 out of one of the fictitious accounts on April 1, 1944, and into the regular Cleveland Chair Company bank account at the branch bank as a deposit on the same day. This deposit represented a payment by Jackson and Alice for the issuance of additional stock in said company to them (1211a). Jackson testified that this was money he had arranged to borrow through Dodd in a regular banking transaction, which borrowing, or the balance of which, was finally paid off at the time of the liquidation of the partnership Jackson Manufacturing Company at year end 1945 (876a-877a, 882a, 893a). Jackson put in evidence in corroboration a series of five $50,000.00 notes signed by himself (Alice joined in two), all payable to the bank on regular bank note forms, the first of same being dated shortly after the date of the $100,000.00 deposit (875a; Exhibit 48; 1116a). Some of

the notes were stamped "paid" with the bank's stamp (877a, 1116a). The bank official through whom the government succeeded in getting the bank records into evidence testified that the notes appeared to represent routine bank borrowing (266a-227a), yet he could find no sign of them on the bank's appropriate liability ledger sheets (all of which were apparently intact, see Exhibits 5-H through 5-M) where they should have been recorded, and he could not explain this (227a).

Evidence totally independent of Jackson's own testimony, which the Tax Court chose to disbelieve (1247a), and of a weight of at least equal to the bank records the government relied upon, corroborated Jackson to this extent:

The regular partnership account at the bank reflected a deposit of a $100,000.00 bank borrowing on December 31, 1945, by Jackson and Alice (Exhibits XXXand 75; 882a). This borrowing was also reflected on the bank's liability ledger (Exhibit 5-I, 882a-883a). Said partnership was thereupon liquidated (the business continued as a corporation) and very substantial sums were distributed to the two partners which were deposited immediately in their respective regular checking accounts at the bank (883a-884a, Exhibits 4-D and 4-G) The bank ledger sheets for Jackson's regular checking account at the bank, introduced by the government, showed a withdrawal on January 6, 1946, in the sum of $27,500.00 (Exhibit 4-D; 884a). A cancelled check in that amount, drawn on said account, in Dodd's handwriting other than Jackson's signature, dated January 7, 1946, made payable to the bank and apparently cashed by it, was among the fragments of records Jackson still had (Exhibit 50, 1118a; 884a). The bank entry and the check, though dated one

day apart, were obviously related, as no other withdrawal in this amount appears (Exhibit 4-D).

The bank ledger sheets for Alice's regular checking account at the bank introduced by the government (Exhibit 4-G, 885a) also show a withdrawal on January 6, 1946, but in the amount of $22,500.00. Alice's cancelled checks for this period had not been retained (1145a). The two withdrawals aforesaid of January 6, 1946, total $50,000.00 and are in the ratio of 55% to 45% - the same ratio as the respective interests of Jackson and Alice in the partnership (885a, 924a-925a). No record of a payment of $50,000.00, or of $27,500.00, or of $22,500.00, at or about January 6, 1946, or otherwise, appears as a credit on any of the bank's liability ledger sheets introduced into evidence by the government (Exhibits 5-H through 5-M).

Meanwhile the $100,000.00 borrowed December 31, 1945, as aforesaid, was according to the appropriate bank liability ledger sheet reflecting it and introduced by the government (Exhibit 5-I) paid in full on January 28, 1946. The bank records introduced by the government further show that this $100,000.00 was repaid on that date by $47,000.00 in withdrawals from Jackson's and Alice's respective checking accounts (Exhibits 4-D and 4-G) and that the balance of $43,000.00 was additional regular bank borrowing (Exhibit 5-J).

There is thus proof of the strongest sort in the record that at a time when the government contends Petitioners had hundreds of thousands of dollars at their disposal in the fictitious accounts, Petitioners Jackson and Alice are engaging in a regular bank borrowing and repaying of $100,000.00, and above all, are making a payment to the bank of $50,000.00 which the bank's liability ledger records introduced by the government, though apparently complete, (Exhibits 5-H through 5-M) fail to reflect,

either as a payment or a previous liability.

Such proof considered "inconsistent and confused" by the Tax Court (1234a-1235a), but not otherwise discussed by it or the Sixth Circuit, has no apparent basis whatsoever for being disbelieved, and strongly corroborates Jackson's sworn testimony (885a, 893a) that he thought he was borrowing from the bank and repaying it instead of obtaining his own funds from the fictitious accounts. It further strongly corroborates Petitioners' theory that through Dodd's manipulations with his side funds in the fictitious accounts, Petitioners have been caught in a web of circumstantial evidence from which thus far they have been unable to extricate themselves. Petitioners challenge the Respondent, should he file a brief in Opposition to this Petition, to explain the proof of the $50,000.00 repayment aforesaid on a basis consistent with Respondent's theory of the case.

Other aspects of the case also cast grave doubt as to whether justice has in fact been done and further point up the critical nature of the burden of proof question.

The bank records of the branch bank for the period when under Dodd's control, which of necessity formed the cornerstone of the government's proof, were so grossly irregular in many respects and had so obviously been tampered with by Dodd, (see cross-examination of bank official Brown through whom they were ultimately introduced at 190a-247a, 275a-276a) that the the Tax Court most reluctantly admitted them at the trial after finding that they were "questionably substantiated" by only a "scintilla of evidence" as having been kept in the ordinary course of business (280a). Neither the Tax Court nor the Sixth Circuit endeavored to explain how bank records so characterized could be the basis of "clear and convincing" evidence in a tax fraud case.

The government investigating agents acknowledged

that the taxpayers voluntarily and immediately made available to the government retained copies of critical tax returns which the government no longer had (368a, Stipulation at 64a, Paragraphs 1-3; *that taxpayers only retained counsel after the government agents had had discussion with them and were "deep into" the case (370a); that the government made no effort to corroborate their findings with a net worth investigation (381a, 470a); that they made no effort to check whether the resulting percentages of gross and net profits to sales could be deemed possible after the alleged deficiencies in income were added into the operating statements of the two businesses, without the addition of the corresponding deductions claimed (382a); that the only likely source of the omitted income was the two businesses (383a-385a, 465a); that they found no evidence or indication of over ceiling sales as compared to purchases (383a, 469a); that they had made no effort to determine the likelihood of the extraordinarily high profit margins resulting from the government's adjustments, in the light of the squeeze between Petitioners' sales at OPA prices and purchases at Black Market prices (384a, 470a-471a); and that it "would be pure conjecture" to say what part of the omitted gross income would be "net" (386a-387a).

---

* The government could not possibly have made out its case without this voluntary act of Petitioners. See Drieborg v. Comm. 225 F. 2d 216 (6th Cir. 1955).

Despite the speculative inferences to be drawn from the apparent relationship between the names given the fictitious accounts and Petitioners (1201a), the Tax Court held that the overall proof in this regard (showing that all deposit slips were in Dodd's handwriting) did not establish that Jackson knew of these accounts as such (1236a-1237a), and the Tax Court accordingly refused to hold Jackson and Alice liable for not including interest income on these accounts in their tax returns in the years barred by the Statute of Limitations (1246a-1248a).

Further, Bank Official Brown testified that bank transit letters upon which the government based its proof as to the omitted checks endorsed by the two companies (Exhibit 5-G, 1201a) would have appeared the same if the companies had cashed the checks at the bank as claimed, and then some person affiliated with the bank (Dodd) had deposited the checks to the credit of his own accounts (243a-244a). He stated that the endorsed checks had become "bearer" instruments and as such they did not require further endorsement (243a-244a, 275a-276a).

Brown also testified that a Government regulation at the time required banks to report substantial deposits of cash, but not of checks (244a-245a), which would supply Dodd with a motive to purchase checks with his own cash and deposit these checks to accounts owned by him. The proof indicated Dodd had a large amount of cash which he needed to convert to a more convenient form for further handling (817a-818a).

Other substantial evidence not dependent upon Jackson's credibility, throwing serious doubt on the government's case and requiring that it be held to the proper burden of proof, was the following:

Unlike the typical tax fraud cases, business income as reported by Petitioners for the years in question was

substantially above industry averages (1219a). In the critical year of 1943, when the most deposits were made to the fictitious accounts, the percentages of net income to sales of the two businesses before taxes were as follows: (1219a):

	Jackson Mfg. Co.	Cleveland Chair Co.
As originally reported	9.57	6.61
As determined by Respondent	27.02	21.33

The industry average for 1943 (Southern Furniture Manufacturers Association) also before taxes, was 6.19 percent (1219a) and as above shown, Petitioners were selling at OPA prices (469a). Perhaps even more incredible is the fact that, based on the Commissioner's own figures for each of these years, Jackson Manufacturing's Net Income Ratio for the year 1943 (the year in which the Commissioner determined the largest deficiency for that company) was more than double its Net Income Radio for the years 1942 and 1945 and almost double that of 1944 (1219a).

Further, Petitioners' proof was that at about the same time Wooten went into the service early in 1944 (1217a), Jackson was able to arrange a line of supply of upholstery material, which became popularly known as "Jackson Velour", which virtually eliminated further need for Black Market transactions (584a-585a, 745a-752a). This would appear self serving until a most peculiar pattern evidences itself upon analysis of the deposits and withdrawals to the fictitious accounts as Petitioners did in their Exhibit 52, consisting of schedules beginning at 1120a. The government agreed with these schedules after minor adjustments not here important (393a-396a).

When the deposits for 1942 through 1949 are analyzed from Exhibit 52 (after the deduction of inter-account transfers, and the ignoring of checks indicated to have been cashed) and then compared with withdrawals, the following results are obtained:

Year	Net Deposits	Withdrawals	Number of Withdrawals
1942	$ 29,223.36	$ -0-	0
1943	423,940.84	79,000.00	5
1944	77,418.43	192,849.96	11
1945	-0-	14,500.00	2
1946	-0-	* 16,489.19	4
1947	-0-	-0-	0
1948	-0-	-0-	0
1949	-0-	36,654.16	8
	**$530,582.63	**$339,493.31	30

* $11,000.00 eliminated (See 395a-396a).

** Net deposits shown exceed withdrawals shown by $191,098.32.

The total net deposits (the original deposit was in June of 1942) as shown by Schedules 4 and 5 of Exhibit 52 through November 24, 1943 were $365,051.35, after the elimination of transfers and ignoring less than $5000 in checks cashed, whereas only a total of $29,000.00 is shown to have been withdrawn through that date, the first withdrawal having occurred on August 12, 1943 (Schedule 8 of Exhibit 52, 1139a).

Obviously if omitted Black Market purchases were being made beginning in 1942, as the Tax Court found (1215a), from the proceeds of cashed company customer checks (491a-493a; 1078a-1079a), but the checks are ending up in the fictitious accounts, with no withdrawals from same until late in 1943, there is circumstantial evidence of the strongest nature to indicate the checks had

been cashed for taxpayers by Dodd with his private funds and thereafter, the checks, now Dodd's in bearer form, were deposited to Dodd's fictitious accounts. Agent Gray assumed the absence of withdrawals meant that omitted Black Market purchases had not occurred as claimed (381a), but the Tax Court did not agree with him, making the $100,000 adjustment aforesaid (1243a).

The Government agents acknowledged that they had wondered about the peculiar pattern shown by the foregoing analysis of the deposits to the fictitious accounts, showing a gradual and comparatively moderate start in 1942, a great expansion in 1943, and then a complete ending of all deposits on January 31, 1944 (390a-392a).*

Thus at a time when net income as reported was at record highs for the two businesses (1224a-1227a) and the motive to cheat should have been continuing unabated, the government's own investigation shows conclusively that all deposits to the fictitious accounts stop as of January 31, 1944, shortly before Wooten went into the Service, and at a time when Jackson testified that the need to buy further on the Black Market virtually ceased. Thereafter the government's analysis of the bank transit letters showed for 1944 approximately $10,000.00 in omitted customer checks cashed and not deposited to the fictitious accounts, and $20,000.00 for 1945. (Exhibit 52, Schedules 6 and 7, 1135a-1137a).

---

* The government investigation of bank records began with the year 1949 and worked backwards to 1945 before finding the first discrepancies (293a-294a).

If tighter controls by his accountant caused Jackson to stop his forbidden activities in 1944 as the Tax Court speculates (1237a) and the proof nowhere establishes, or if Jackson was otherwise frightened, why did he hold some of the accounts open until 1949 when the last withdrawals were made as above shown? Why did he not panic when Dodd was transferred from the branch bank in 1946 to a bank at Cedartown, Georgia (870a-871a) and close out the accounts at that time since he would appear to have lost the only insider through whom he had access to the accounts?

The involved side financial transaction (1212a-1213a) Dodd arranged and got Jackson into at the time of the $100,000 stock purchase discussed above (See 857-873a) makes no sense whatsoever other than as a subterfuge concocted by Dodd for his own devious purposes, possibly to keep Jackson unaware of the true source of the funds he was receiving. Why would Jackson try to take concealed funds from the branch bank and "hide" same in his own name in an obscure St. Augustine, Florida bank run by Dodd's brother, and take a deduction on his 1944 income tax return as filed for interest paid this bank, identifying same by name (399a, 867a), when the least inquiry by the government would have led through the St. Augustine Bank records straight back to the branch bank in Chattanooga and potential disaster for Jackson if guilty? After the funds were transferred at Dodd's request from St. Augustine to a bank in Rome, Georgia, along with Dodd's now deceased brother, the proof was uncontradicted that Dodd ultimately got both the principal and the interest (93a, 870a-873a).

If Jackson had anything to hide with respect to the seven specific transactions relied upon by the Commissioner, it is again very strange that a clear lead to the second most important of the seven transactions involved, the

$50,000.00 withdrawal at the time of a farm purchase (1210a-1211a), was to be found in the returns as filed for the years in question. Jackson claimed this transaction involved a $40,000.00 loan from Jackson's father, with the funds having been given to Dodd to handle (847a-855a, Exhibit 51, 1119a, 844a, 848a, 1051a, 360a-361a). The individual income tax returns of Jackson and Alice for both 1944 and 1945 claimed interest deductions listing Jackson's father as the party to whom the interest was paid on this loan (850a). The slightest questioning by the Government of this claimed deduction would obviously have led the agent into a transaction which the Government's theory indicates Jackson could only have wished to keep secret.

Both the Tax Court (1237a) and the Sixth Circuit (A7) commented on the fact that although Dodd was present in the courtroom throughout the trial, neither party elected to call him as a witness.

Finally, and perhaps most important of all to this petition, is the finding by the Tax Court that the deficiencies as determined by Respondent were erroneous, whereupon the Tax Court seized upon an obscure hearsay statement in the record, and it alone, to "rehabilitate" the government's case (A 12), by further finding that after allowing Petitioners an additional $100,000 in deductions for Black Market purchases, the government's determinations should otherwise be sustained (1217a, 1221a-1222a, 1235a, 1239a, 1243a).

At the trial witness W. E. Wooten (then a competitor 602a-603a), who had handled the Black Market purchasing for both businesses prior to his entry into the service in 1944 as aforesaid, testified that he personally pulled and cashed all the omitted checks during that time and every penny was used for purchases of materials (496a-497a, 539a). On cross examination he stated he

did not remember telling Internal Revenue Agents in Johnson City, Tennessee, in May of 1952 that the amount of Black Market purchases was between 75 and 100 thousand dollars, and stated that any estimate he might give would be a "sheer guess" (582a-583a). Agent Gray in rebuttal later testified Wooten had made such a statement to him (1089a-1090a) but acknowledged that it had been made at the moment, without any reflection on Wooten's part and was merely an estimate (1091a). Of course this was hearsay on Gray's part since Gray had no personal knowledge at any time as to the truth or accuracy of the statement.

The Sixth Circuit found in this regard as follows: (A3)

> "The Tax Court here found that only $100,000 of the more than half-million-dollar unreported gross income was applied to black market purchases. Thus this finding left over $400,000 of admittedly unreported gross income unexplained and unaccounted for. It is appellant's main argument that the evidence from which the Tax Court made this finding was not the sort of 'clear and convincing' evidence necessary for a finding of fraud.
>
> "We are not unimpressed with this contention. The Tax Court employed an estimate as to the total of appellant's black market purchases which was made to an Internal Revenue Agent at the first interview of appellant's office manager, W. E. Wooten. Subsequently, at trial this same witness testified strongly for appellant that every dime of the funds he withheld was spent on black market purchases. While Wooten did not deny making the estimate previously referred to, he declined at the time of trial to attempt such an estimate. If the facts referred to up

to this point constituted the sole evidence of fraud, we might not conceive it to be the sort of 'clear and convincing' evidence required to avoid the statute of limitations."

The government obviously tried the cases on the misconception that once it had established omissions of gross income (which the taxpayers never contested) the burden shifted to the taxpayers to prove their claimed offsetting deductions -- otherwise gross income would become net income (468a-469a, 471a). Thus although the government agents freely conceded that their investigation indicated Black Market purchasing had occurred (378a-379a), they allowed no deductions for same whatsoever, reasoning that until the taxpayers proved entitlement to such deductions, the government's determination must stand (468a-469a). Having established that the government's deficiency determinations were wrong, but having no records remaining through no fault of their own to support their sworn contention that all omitted sales were offset completely by omitted purchases, Petitioners have no choice but to rely upon the rules as to burden of proof, and challenge the government to show proper proof anywhere in the record which establishes that any deficiency of net income exists and if so, the correct amount.

REASONS FOR GRANTING THE WRIT

Introductory Statement

This case involves an important area of the law badly in need of further clarification by this Court. It is believed that the subject Sixth Circuit decision is in conflict with the controlling decision of this Court in Helvering v. Taylor, 293 U.S. 507, decided in 1935. The various case citators show that a multitude of United States Court of Appeals decisions and lower court decisions have since 1935 passed upon burden of proof problems in tax cases, where they are uniquely prevalent, commonly citing Helvering v. Taylor as authority for the particular position taken. No subsequent decision of this Court, however, so far as Petitioners have been able to discover, has dealt substantially with the field traversed in Helvering v. Taylor, now 37 years old, and Shepard's United States Citations shows only four decisions of this court which have even cited the case, none of which are here material.

Without further guidance from this Court since 1935 in this busy area of the law, sharp conflicts have crept into the lower court decisions, as will be hereinafter demonstrated, the proper resolution of which is critical to a proper decision in the subject cases. This Court has not hesitated previously to grant certiorari in an income tax case where conflict was shown on the issues involved between the various Courts of Appeals Corn Products Refining Co. v. Comm., 350 U.S. 46 (1955).

Taxpayers were at an extreme disadvantage in these cases due to the innocent and virtually complete loss of their decisive vital records. With the great passage of time involved, it was inevitable that the human memory of those that still survived would not permit complete and

perfect answers in all cases, particularly in the absence of records. As was stated in Delone v. Comm., 100 F. 2d 507, (3rd Cir. 1938):

> "Explanations which would have been expected and might have been called for of a recent transaction, may well be excused after such a lapse of time as existed here. This has a bearing upon the question of actual fraud."

Despite some concern on the part of the Sixth Circuit as to the taxpayers' special difficulties due to the passage of time (A6), it is submitted that both it and the Tax Court declined to show any such consideration to the taxpayers as they might have expected under Delone (supra). It is also well to bear in mind, when considering the three questions presented, the statement of this Court in Burnet v. Houston, 283 U.S. 223 (1931), as follows:

> "The impossibility of proving a material fact upon which the right to relief depends, simply leaves the claimant upon whom the burden rests with an unenforceable claim, a misfortune to be borne by him, as it must be borne in other cases, as the result of a failure of proof."

The confusion as to where the burden of proof lies in a tax case, and particularly a tax fraud case, despite many well established and unquestioned rules, is aptly illustrated by the four-step development of the problem in this case:

(1) The Government tried this fraud case on the theory that once it had shown omissions of gross income, the burden shifted to the taxpayers to prove their deductions and establish correct net income (469a).

(2) The Tax Court agreed with the Government and held

that despite its finding that the Commissioner's determinations were erroneous, "the burden of proof as to the amount of deficiency is on the Petitioners, and Petitioners have totally failed to carry this burden" (1247a).

(3) The Government brief in the Sixth Circuit (an excerpt from which has been certified in the record and appears in Appendix A hereto) acknowledged the error of the Tax Court in this regard (A12). It claimed, however, that the Commissioner's erroneous determination "that there had been no black market purchases" was "rehabilitated" by the proof introduced by the Government, based upon which the Tax Court made the $100,000.00 adjustment, "inasmuch as taxpayer did not then meet his burden of rebutting it" (A12). It was there further stated that a "taxpayer never loses his burden of showing that the Commissioner's determination is wrong" and that "the burden remains on the taxpayer to discredit the Commissioner's extrinsic proof." (A12).

(4) The Sixth Circuit apparently agreed with the Government's said brief, for it held that even though the Commissioner's redetermination had been to an extent overturned by the Tax Court's allowance of an additional $100,000 in Black Market purchases, nonetheless, this fact did not shift "the burden of proof as to total taxes due back to the Commissioner" (A6). Instead, the Sixth Circuit stated that "it seems clear to us, however, that the burden of proving the amount of the claimed Black Market deductions was on the taxpayers" (A6).

It is respectfully submitted that both the Government and the two lower courts have erred in their respective positions at each of the four stages of this case as above described, as will be hereinafter shown.

Question One

It is recognized that once the Commissioner has established by clear and convincing evidence in a fraud case otherwise barred by the Statute of Limitations, that at least part of an asserted deficiency is due to fraud, the taxpayer then has the burden, as in a non-fraud case, of going forward with the necessary proof to show that the Commissioner's deficiency determination is erroneous and thereby overcoming the presumptive correctness of same. Bryan v. Comm., 209 F. 2d 823, (5th Cir. 1954), Kreps v. Comm. 351 F. 2d 1 (2d Cir. 1965).

In Helvering v. Taylor, 293 U.S. 507, (1935), aforesaid, this Court bound the Sixth Circuit and all other lower courts with the following words:

> "We find nothing in the statues, the rules of the board or our decisions that gives any support to the idea that the commissioner's determination shown to be without rational foundation and excessive will be enforced unless the taxpayer proves he owes nothing or, if liable at all, shows the correct amount. While decisions of the lower courts may not be harmonious, our attention has not been called to any that persuasively supports the rule for which the commissioner here contends.
>
> "Unquestionably the burden of proof is on the taxpayer to show that the commissioner's determination is invalid. Lucas v. Structural Steel Co., 281 U.S. 264, 271, Wickwire v. Reinecke, 275 U.S. 101, 105, Welch v. Helvering, 290 U.S. 111, 115. Frequently, if not generally, evidence adequate to overthrow

> the commissioner's finding is also sufficient to show the correct amount, if any, that is due. See, e.g., Darcy v. Commissioner, 66 F. (2d) 581, 585. But, where as in this case the taxpayer's evidence shows the commissioner's determination to be arbitrary and excessive it may not reasonably be held that he is bound to pay a tax that confessedly he does not owe unless his evidence was sufficient also to establish the correct amount that lawfully might be charged against him.

Thus, a taxpayer, having shown the Commissioner's deficiency determination to be invalid has no further burden to go forward and show, in addition, that he owed no tax, or the correct amounts to be charged against him. Helvering v. Taylor, (supra); Grubb v. Comm., 315 F. 2d 753, (6th Cir. 1963); Welch v. Comm., 297 F. 2d 309 (4th Cir. 1961). It then becomes "the Commissioner's burden to prove that the determination was correct in spite of the errors shown" Thomas v. Comm., 266 F.2d 297 (6th Cir., 1959).

> "In short, the Commissioner's determination is presumed correct, but if error is shown, the presumption disappears and the Commissioner then has the burden of proving the correctness of his determination, or at least the correct amount actually due. A presumption is but a heavier burden of proof, but once overcome the burden of going forward shifts with the introduction of the proofs." Harp v. Comm., 263 F. 2d 139 (6th Cir. 1959). (Emphasis Supplied)

It is submitted that the Sixth Circuit decision in the instant case on this phase of the problem is not only in con-

flict with its own decision in Harp v. Comm., (supra), but also with that of the Fourth Circuit in Welch v. Comm., 297 F. 2d 309 (4th Cir. 1961) (supra), where the Court stated:

> "the Commissioner's rejection of these deductions in toto was plainly wrong. In short, the presumption of correctness to which the determination of the Commissioner is ordinarily entitled was destroyed by its own inherent defect. Under these circumstances the burden of proof did not rest upon the taxpayer, and the Tax Court was not justified in basing its decision upon the failure of the taxpayer to show the precise amount of the deductions to which he was entitled."

Taxpayer's proof was, in the above quoted language of Helvering v. Taylor "adequate to overthrow the Commissioner's finding" (both lower courts so held), but unlike some cases was not "sufficient to show the correct amount, if any, that is due", unless the sworn claim that all omitted sales were offset by omitted purchases be accepted. The Government's brief in the Sixth Circuit recognized by implication that if the Sixth Circuit rejected the $100,000.00 adjustment, then despite proof of fraud, the ultimate decision must be for the taxpayers. (A12).

This is in accord with the Tax Court's summary of the "line of cases headed by Helvering v. Taylor," that once the determination of the Commissioner is deemed arbitrary and excessive, "there is no burden on the taxpayer to show the correct amount of tax, and if neither party can show the correct amount, then there can be no deficiency." (Emphasis Supplied). J. D. Farber, 43 TC

407, Dec. 27, 201. It is also worth noting that here the error affected the entire deficiency, rather than a separate part of it, as in Hoffman v. Comm., 298 F. 2d 784, (3rd Cir. 1962). Hence no part of the presumption of correctness can remain.

It is apparent that the Sixth Circuit regarded with substantial disapproval the Tax Court's hearsay evidence basis for the arbitrary $100,000.00 adjustment it made (A3). This Court commented in a similar situation in Consolidated Edison Co. v. NLRB, 305 U.S. 197, 230 (1938), that "Mere uncorroborated hearsay or rumor does not constitute substantial evidence" to support a finding made even by an administrative tribunal.

It is accordingly submitted that there is no proper basis upon which the proposed "rehabilitating" (A12) adjustment by the Tax Court can be upheld. It is thus taxpayers' further contention that they have brought themselves squarely within the rule of Helvering v. Taylor in that they have destroyed the presumptive correctness of the Commissioner's deficiency determination, and the Commissioner has failed to introduce any competent proof to carry his resulting burden of showing the correct amount due.

If it were assumed, however, that there was a proper basis for the $100,000 adjustment or any other adjustment in the evidence, the Government's Sixth Circuit brief argues as follows (A12):

> "The point that taxpayer misses is that a taxpayer never loses his burden of showing that the Commissioner's determination is wrong, and that if the Commissioner can support his deficiency determination even without the aid of the presumption of correctness the burden

remains on the taxpayer to discredit the Commissioner's extrinsic proof. United Aniline Co. v. Commissioner, 316 F.2d 701, 704 (C.A. 1st). Taxpayer here clearly failed to do this."

The United Analine decision, cited by the Government, was decided in 1963. It recognized and pointed out the differences of opinion between the various Courts of Appeals in this problem area in the following words:

"...this argument involves a serious misconception on taxpayers' part. We agree with them that the Commissioner's determination of amounts is not 'evidence.' But we cannot agree with those courts which appear to say that it merely shifts onto the taxpayer the 'burden of going forward with evidence,' see, e.g., Stout v. Commissioner, 4 Cir., 1959, 273 F. 2d 345, 350, or that it creates a presumption which 'disappears' in the face of positive evidence. Stout v. Commissioner, supra; Gersten v. Commissioner, 9 Cir., 1959, 267 F. 2d 195, 199. While it may not be uncommon to use the word 'presumption,' it must be done only when it is made clear that the taxpayer never loses the burden of proving the Commissioner's determination erroneous. See Sharaf v. Commissioner, 1 Cir., 1955, 224 F. 2d 570, 572. The danger of speaking of presumptions in isolation is that it may lead to the error illustrated in Clark v. Commissioner, 9 Cir., 1959, 266 F. 2d 698, of concluding that if taxpayer introduces evidence from which it

'could' be found that the Commissioner's determination was erroneous the 'disappearance' of the presumption places the burden of proof on the Commissioner. Id. at 706."

United Aniline also conflicts with the Eighth Circuit in Cullers v. Comm., 237 F. 2d. 611, (8th Cir. 1956) which held that the presumption "vanishes" in the face of substantial evidence to the contrary. The First Circuit opinion is also to be sharply contrasted (along with the Government's above quoted position that "a taxpayer never loses his burden of showing that the Commissioner's determination is wrong") with the opinion of the Fifth Circuit in Cohen v. Comm., 266 F. 2d 265, (5th Cir. 1959) where it stated the following:

"Respondent argues that the taxpayer did not meet his burden of showing that the Commissioner's determination, 'as redetermined by the Tax Court,' was arbitrary or invalid. The question, however, is not whether this determination was invalid after the Tax Court had reduced it by eighty-five per cent. The pertinent inquiry is whether it was invalid as originally computed by the Commissioner. See Helvering v. Taylor, supra, p. 515. Respondent has not here claimed that the Commissioner's original determination was valid.

"Cohen, having met his burden of proving the Commissioner's determination invalid, and thus taking the presumption of the correctness of that determination out of the case, was not chargeable with failure to make a further showing. Hence it was improper for the Tax Court in making its redetermination to accept its maximum

possible gross income figure as the actual figure only because Cohen failed to show a lesser amount." (Emphasis Supplied)

See also MacCrowe's Estate v. Comm., 252 F. 2d 293, (4th Cir. 1958), which held that once the Tax Court rejected the Respondent's deficiency determination and redetermined same, the presumption as to the correctness of such determination was out of the case.

The subsidiary issue involved, should this Court somehow uphold the $100,000.00 adjustment, is thus whether the burden stayed with the Commissioner once his basic determination is shown to be erroneous, even after "rehabilitating" proof was offered, or whether thereafter the burden again shifted back to the taxpayer who had already carried the day as to the original deficiency determination. As shown above, a square conflict of substantial proportions exists between the Courts of Appeals on this question, and the Sixth Circuit in the instant case has aligned itself with those courts who favor the Government rather than the taxpayer.

An obvious appeal can be made to "fundamental notions of fair play" in support of those decisions favoring the taxpayer on this point, as being essential to our overall scheme of voluntary taxation in this country. It is accordingly respectfully submitted that the answer to Question One should, in accordance with the principles announced in Helvering v. Taylor, be in the negative and the Sixth Circuit should be reversed on this point.

Question Two

The previous question assumed that the requisite proof of fraud had been established (which Petitioners deny) thereby overcoming the Statute of Limitations. This question and the Third Question raise issues as to the burden of proving or

disproving the claimed offsetting deduction, in the context of the Government's statutory burden of proof in a fraud case (26 U.S.C., Section 7454(a), supra), which the Courts have uniformly held means proof by "clear and convincing evidence". Kreps v. Comm. 351 F. 2d 1 (2d Cir. 1965).

Here again there is a sharp conflict in the decisions in the lower courts.

The Sixth Circuit recognized that the respondent had the burden of not only showing apparently fraudulent conduct, but also of showing in addition that "some portion of the tax deficiency is due to fraud" (Emphasis Supplied) (A5). See also Cirillo v. Comm., 314 F. 2d 478 (3rd Cir. 1963) where the Court stated that "a fraud penalty can be imposed only where proof of a deficiency is supplemented by proof that the 'deficiency is due to fraud with intent to evade tax'."

Unless therefore, Respondent can establish that some net income, as compared to gross income, has been omitted, he will not have established a "tax deficiency" and will not have carried the second part of the two-part burden imposed upon him in a fraud case prerequisite to overcoming the Statute of Limitations. Until this has occurred, there is no presumption in favor of the Commissioner's deficiency determination if otherwise barred by the Statute of Limitations. Drieborg, et al v. Comm., 225 F. 2d 184, (6th Cir. 1955); George v. Comm., 388 F. 2d 221 (1st Cir. 1964).

The Sixth Circuit decision in the instant case (A6) erroneously relieved the Commissioner of its burden in a fraud case of first proving that a tax deficiency had in fact occurred and instead placed upon the taxpayers the burden of proving the opposite before a presumption had arisen in favor of the Respondent's deficiency determination.

The following decisions are in conflict with the Sixth Circuit on this issue:

(1) Richardson v. Comm., 264 F. 2d 400 (4th Cir. 1959)

wherein the Court made the following statement:

> "We cannot agree that the finding of an understatement of gross receipts automatically puts on the taxpayers the obligation to prove the offsetting deductions in order to escape a fraud penalty. Such a contention might have more force in a case where the unreported income and deductions were unrelated or only remotely related.
>
> ***
>
> "In order for a fraud penalty to be assessed where the unreported items of income and expense are closely related, the Commissioner must prove that at least some unreported net income resulted from the unrecorded transactions.

(2) Ries v. U. S., 172 F. Supp. 929 (E.D. Pa. 1959) wherein the Court stated:

> "The Government has not established by the quantum of proof required in a fraud case that the case purchases claimed to have been made by the taxpayers were fictitious. There is therefore no evidence sufficient to shift the burden of going forward to the taxpayers. The Government cannot use the taxpayers' failure to prove that the payments were in fact made when the Government has introduced no evidence sufficient to sustain the burden which it carried to establish the contrary. To hold otherwise would be to relieve the Government of the burden of proving fraud and to require the taxpayers to sustain the burden of disproving it."

(3) Lloyd J. Lowe, T.C.Memo. 1955-150, 14 T.C.M. 547,

wherein the Tax Court stated:

> "Here, however, respondent has employed the bank deposits method which, in the case of a taxpayer in a trade or business, is more indicative of gross receipts than it is of net income. Where respondent resorts to the latter method, in order to affirmatively prove fraud he must also prove that the taxpayer's allowable deductions do not exceed an amount which, when deducted from gross income, leaves a substantial amount of unreported net income."

In addition to the foregoing three cases, it appears that one of the Sixth Circuit's own decisions conflicts with its decision in the present case. See Grubb v. Comm., 315 F. 2d 753 (6th Cir. 1963, supra) where it was held that the Tax Court erred in holding that the burden was on the taxpayer to establish what amounts of cash he had on hand at the end of the various years in question, after the Tax Court had found that the Commissioner was mistaken in his computations as to Petitioner's cash on hand.

Masters v. Comm., 243 F. 2d 335 (3d Cir., 1957), and Clark v. Comm., 226 F. 2d 698 (9th Cir. 1959), appear to be in conflict with the Richardson decision (supra) in that they required the Commissioner to prove only that sales were understated. Jack M. Chesbro, 21 T.C. 123 (1953) aff'd per curiam, 225 F. 2d 674 (2d Cir. 1955) apparently agreed with Richardson v. Comm., supra, since that decision turned in large part upon the fact that the Commissioner had proved not only that sales were understated, but also that "the purchases were not understated in amounts at all comparable thereto", which latter fact the Respondent did not even bother to undertake to

prove in the instant case (468a-469a, 471a). This was undoubtedly due to the Government's fundamental misconception at the outset that its only obligation was to establish omissions of gross income (which the taxpayers at all times freely admitted), whereupon it could rest its case and enjoy the spectacle of the taxpayers attempting to do the impossible of corroborating their sworn testimony, in the absence of the precise records they once had.

There is thus a square conflict of opinion in the lower courts as to whether in a fraud case, the Commissioner, having established omissions of gross income, must also do the necessary to prove that some net income resulted, before the necessary finding can be made that fraud with intent to evade tax existed, removing the bar of the Statute of Limitations.

Until a proper decision has been reached, correctly determining the amount of offsetting Black Market purchase deductions to which Petitioners are entitled, then as will be hereinafter argued in Question Three, it is improper to nonetheless conclude that the $184,000.00 in the fictitious accounts traceable, or apparently traceable to the Petitioners were in fact their own funds, as compared to belonging to or otherwise being controlled by Dodd. In the present state of the record, with the strong explanatory proof offered by Petitioners, it was sheer speculation for the lower courts to resolve all doubt against Petitioners, particularly when a proper resolution of this deduction question had yet to occur.

> "Where unimpeached, competent, and relevant testimony on behalf of a taxpayer is uncontradicted, it may not be arbitrarily discredited and disregarded, and the Tax Court cannot reject or ignore this evidence." Tank v. Comm., 270 F. 2d 477 (6th Cir. 1959).

It is thus apparent that should this Court resolve the existing conflict in the lower court decisions above cited by overruling the Sixth Circuit opinion in this case, and following the line of cases headed by Richardson v. Comm., (supra), then (a) the admission by the Government that they recognized that Black Market purchases had occurred. (378a-379a), plus (b) the Tax Court's finding that the Commission's determination that there had been no Black Market purchases was unjustified (A12), coupled with (c) a complete failure of the Government to establish by proper proof as compared to suspicion that any net income was omitted, must result in a decision in favor of the taxpayers. The necessary tax deficiency will not have been established, without which one of the essential elements of a fraud determination, necessary to remove the bar of the Statute of Limitations, will not have been proved.

Taxpayers accordingly contend that the answer to Question Two should be in the affirmative.

Question Three

This question raises the fundamental issue, related to the issue in the previous case, of whether the Sixth Circuit Opinion which this Court is being requested to review, erroneously relieved the Respondent of a part of his overall burden of proof essential to establishing fraud with intent to evade tax, and correspondingly shifted to Petitioners a burden of disproving which the law does not impose upon them.

The Sixth Circuit, while apparently rejecting as being unsupported by proper evidence the Tax Court's windfall "rehabilitation" of the Government's defective case through the $100,000.00 adjustment, instead chose in turn to "rehabilitate" the Government's case by viewing the seven specific transactions adversely to the taxpayers and finding that this proof was sufficient to overturn the Statute of Limita-

tions, and to impose on taxpayers a burden of proving any additional deductions over those allowed them by the Tax Court. As Petitioners analyze the Tax Court Opinion, the Tax Court apparently reasoned that the seven specific transactions established fraudulent intent, but in and of themselves were insufficient to establish a specific tax deficiency, or in other words, specific omissions of net income as compared to gross income. Both the Tax Court and the Sixth Circuit, viewing as they did the seven specific transactions as being fraudulent, thereupon shifted the burden of establishing deductions (and hence net income) to the taxpayers.

It is thus apparent that if, under proper rules of sequence in burden of proof, the seven specific transactions may not be relied upon until there first has been a resolution favorable to the Government of an essential preliminary question, and this preliminary question cannot be resolved favorably to the Government, then the circumstantial evidence indicating fraud on the part of the taxpayers inherent in the seven specific transactions (even if taxpayers cogent explanations are to no avail) cannot be relied upon by the Government.

The Government had the basic burden of establishing fraud. It chose to rely entirely on circumstantial evidence based on grossly irregular (190a-247a) bank records "questionably substantiated" by only a "scintilla of evidence" as being admissable (280a). Neither lower court would comment upon the basic propriety of holding the taxpayers liable on a case built on this unclear and unconvicing quicksand. These records had been under the personal control of Dodd as branch bank manager during the critical years in question and were in such shape that Bank Official Brown, through whom they were introduced, would not attempt to testify which if any were true bank records and which were Dodd's private records kept on

bank forms (239a). He further agreed there were grounds for viewing the bank records with a "great deal of suspicion" (241a). Under these circumstances, the Government, despite having the basic burden of proof, still relied on its circumstantial evidence and chose not to call Dodd to the stand, though he was available at all times in the Courtroom (1237a, A7). Not a single witness on either side testified of their own knowledge that any of the Petitioners were linked to the fictitious accounts, nor were there any signatures, deposit slips, or other handwriting evidence creating such a link. Under the circumstances, the Government's reliance solely upon circumstantial evidence and its declining to put witness Dodd on the stand (whose position had already been indicated in the record as favorable to taxpayers (377a), must be resolved most strongly against the Government, which had the burden of proof.

The decisions of the Tax Court and the Sixth Circuit in this case placed the cart ahead of the horse. They permitted the Government to rely upon circumstantial evidence of suspicious facts to transfer the burden of proof to the taxpayers of proving their deductions, instead of imposing upon the Government the initial burden of disproving the claimed deductions, and thereby establishing a specific tax deficiency, which the Government made no effort to accomplish by proper proof. If the taxpayers' sworn testimony claiming a complete offset be discounted by that solemn process whereby one human being vested with judicial power is permitted in our legal system to intuitively state that another human being's testimony is not worthy of belief (and thereby avoiding coming to grips with the merits of the testimony), nonetheless, a vacuum still exists both ways on the offsetting deduction question. The result is that as a matter of law, the party who had the burden of proof fails and the other party prevails. Burnet v. Houston, 283 U.S. 223 (1931) (supra).

"Since the burden was on the Commissioner to prove fraud, it must follow that he had the burden of proving every subsidiary fact relied upon by the court to support that ultimate conclusion. To permit, in satisfying this burden, the use of a Commissioner's finding that was to be accepted only because the taxpayer had failed to meet a burden of overcoming it, would be to allow the Commissioner to raise himself by his own bootstraps."
George v. Comm., 388 F. 2d 221, (1st Cir. 1964).

"Although the existence of fraud may be gathered from circumstances, the piling of inference upon inference hardly qualifies as the clear and convincing evidence by which fraud must be proved." Goldberg v. Comm., 239 F. 2d 316 (5th Cir. 1956).

"The Commissioner's heavy burden of proof on the issue of fraud cannot be satisfied by mere disbelief of taxpayer's testimony. The record must contain some convincing affirmative indication of the required specific intent."
Cirillo v. Comm., 314 F. 2d 478, (3rd Cir. 1963).

The Sixth Circuit in the instant case in its Opinion recognized the problem involved when it stated (A6):

"And, of course, the fact that the Commissioner erroneously failed to allow this $100,000 item did not mean that other determinations not dependent thereon were deprived of the presumption of correctness." (Emphasis Supplied).

It is taxpayers' position that the Commissioner's determination of fraud as based upon the seven specific transactions was dependent upon the Commissioner first carrying his burden of proof of disproving the claimed offsetting deductions which he failed to do. As a matter of cold logic, the Tax Court and the Sixth Circuit have permitted "the Commissioner to raise himself by his own bootstraps" George v. Comm. (supra).

It is again respectfully insisted that the lower courts both erred as specified and that the answer to Question Three should accordingly be in the negative.

CONCLUSION

For the foregoing reasons, this petition for a writ of Certiorari should be granted.

Respectfully submitted,

RICHARD P. JAHN
Tanner & Jahn, Attorneys
12th Floor Volunteer Building
Chattanooga, Tennessee

Counsel for Petitioners

October 9, 1967